

Commission "broad authority to investigate regulated entities"⁹¹ and serves as "the formal means, i.e. **subpoena**, to obtain books, records and information."⁹²

The Commission's staff is authorized to exercise §403 power under delegated authority.⁹³ "The decision to investigate, moreover, is not purely discretionary ... 'where, as in the instant case, the Commission has reason to believe a licensee may be violating the **Act** or its policies, rules and regulations, ... it has a responsibility to inquire and determine whether, in fact, such activity is occurring.'"⁹⁴

A. WorldCom's Public Admissions And The Known Facts Surrounding Its Scandals Reveal A Deep-Rooted Culture Of Fraud And Deception That Makes It A Prime Example Upon Which To Base Rules And Policies.

WorldCom's bankruptcy is unprecedented—not only because of the immense amount of money involved, but because the bankruptcy is a direct result of deliberate, blatant and outrageous fraudulent acts carried out by the company's senior management." While the entire scope of WorldCom's wrongdoing is not yet known, the facts already discovered—many of

⁹¹ SBC Communications, Inc., *Apparent Liability for Forfeiture*, 17 FCC Rcd 7589, 7592 (2002)

⁹² James A. Kay, Jr., Licensee of One Hundred Fifty Two Part 90 Licenses in the Los Angeles, California Area, *Memorandum Opinion and Order*, 17 FCC Rcd 8554, 8556 (2002).

⁹³ *Id.*, citing PTL of Heritage Village Church and Missionary Fellowship, Inc., 71 FCC 2d 324 (1979).

⁹⁴ *Id.*, citing PTL of Heritage Village Church and Missionary Fellowship, Inc., 71 FCC 2d at 327.

⁹⁵ *WorldCom, Inc. Hearings Before the S. Comm. on Commerce, Science and Transp.*, 107th Cong. (July 30, 2002) (indicating that there is a "direct link" between "past accounting irregularities" and WorldCom's bankruptcy) at <http://www1.worldcom.com/infodesk/statements/073002/>.

which have been admitted by the company—reveal that WorldCom’s actions were deliberate and calculated⁹⁶

On June 25, 2002. WorldCom admitted unprecedented accounting irregularities—irregularities intended to make the company look profitable when it was not. Specifically, WorldCom admitted that “certain transfers from line cost expenses to capital accounts...were not made in accordance with generally accepted accounting principles (GAAP).”⁹⁷

B. The Public Interest Demands Institution of a Section 403 Proceeding

Given the glaring evidence of WorldCom’s wrongdoing, the Act, well-settled Commission policies, and the public interest demand that the Commission immediately institute an inquiry pursuant to Section 403 of the Act to fully explore the nature and extent of corruption and wrongdoing that was fostered by the WorldCom, Qwest and Global Crossing corporate cultures. OC-UCC recognizes that other concurrent investigations are currently underway or recently completed at the Securities and Exchange Commission and in Congressional hearings surrounding the Sarbanes-Oxley Act of 2002. However, the SEC investigation can be expected

⁹⁶ In addition to all of WorldCom’s admissions of fraud and criminal indictments, in March 2002 the SEC investigated loans in excess of \$366 million that WorldCom made to Mr. Ebbers, which were “the largest a publicly traded company has given to an officer in recent memory.” Deborah Solomon and Rebecca Blumenstein, Ebbers’s Downfall Came in the Form Of \$366 Million in WorldCom Loans, *WALL ST. J.*, May 1, 2002. On March 11, 2002, the SEC requested information regarding loans from WorldCom to its corporate officers. WorldCom Receives SEC Inquiry, WorldCom Press Release, March 11, 2002, available at <http://www1.worldcom.com/global/about/news/news2.xml?newsid=2010&mode=long&lang=en&width=530&root=/global/about/&langlinks=off> (last visited Sept. 16, 2002). This probe led to the eventual resignation of Mr. Ebbers on April 30, 2001. WorldCom Inc. Announces Executive Changes, WorldCom Press Release, April 30, 2002, available at <http://www1.worldcom.com/global/about/news/news2.xml?newsid=2491&mode=long&lang=en&width=530&root=/global/about/&langlinks=off> (last visited Sept. 16, 2002).

⁹⁷ WorldCom Announces Intention to Restate 2001 and First Quarter 2002 Financial Statements, WorldCom Press Release, June 25, 2002, available at <http://www1.worldcom.com/global/about/news/news2.xml?newsid=3230&mode=long&lang=en&width=530&root=/global/about/> (last visited Sept. 16, 2002) (“WorldCom June 25 Press Release”).

to focus on issues surrounding securities fraud. The Sarbanes-Oxley Act, already law, addresses matters related to protecting shareholders and investors. Neither of these has as yet uncovered the full extent of corporate corruption or proposed remedies that relate to the special issue of telecommunications policy entrusted by Congress to the FCC, and neither has been nor can be expected to be concerned with such issues.

As detailed above, by Congressional design such matters fall to the special expertise and interests of the FCC. Moreover, the SEC's regulations are designed to protect shareholders and investors, whose interests may not necessarily be congruent with the interests of the ratepayers falling within the FCC's jurisdiction.

Further, OC-UCC. recognizes that the Commission usually restricts its inquiry into non-FCC misconduct to "adjudicated" misconduct. However, in this case the need to develop guidance for the telecommunications industry is at a crisis point. Moreover, at least some of the misconduct can be considered to be adjudicated. David F. Myers, the Senior Vice President and Controller of WorldCom during the pertinent time period, pled guilty on September 26, 2002 to conspiracy to commit securities fraud, securities fraud, and false filings with the SEC.⁹⁸ The Honorable Richard Conway Casey of the U.S. District Court, Southern District of New York, accepted the guilty plea and directed the preparation of a pre-sentencing report.⁹⁹ Sentencing has been scheduled for December 26, 2002.¹⁰⁰ More recently, Buford "Buddy" Yates, WorldCom's former accounting director, pled guilty on October 7, 2002 to two counts of securities fraud and

⁹⁸ United States v. Myers, *Plea*, Case no. 02 Cr. 1261 (S.D.N.Y. Sept. 26, 2002).

⁹⁹ *Id.*

¹⁰⁰ *Id.*

conspiracy.¹⁰¹ According to reports, two employees under Mr. Yates are also likely to plead guilty.¹⁰²

Accordingly, a federal criminal case against a former officer of WorldCom has been adjudicated. As discussed previously, Mr. Myers' conduct is attributable to WorldCom.'"

In any event, as the Commission held in *Character Policy Qualifications*, where the conduct hearing on character is "so egregious as to shock the conscience and evoke almost universal disapprobation," the FCC may consider the effect of the conduct before the matter is adjudicated.¹⁰⁴ The notorious conduct at issue in this case – what has been called the "largest instance of corporate fraud in the history of U.S. commerce" – surely meets this standard.¹⁰⁵

The Commission has ample authority to initiate an inquiry.¹⁰⁶ The facts and circumstances demand that it exercise that authority in the context of the requested rulemaking.

¹⁰¹ Ben White, WorldCom Officer Pleads Guilty to Fraud, *Washington Post*, Oct. 8, 2002, at E01.

¹⁰² Id

¹⁰³ 47 U.S.C. § 217.

¹⁰⁴ Character Policy Qualifications, 102 FCC 2d at 1205.

¹⁰⁵ Christopher Stern & Kathleen Day, U.S. Ready to Charge WorldCom Ex-Officers; Ebberts May Be Among Target, Source Says, *The Washington Post*, July 26, 2002.

¹⁰⁶ "By virtue of [§ 403's provisions and mandate], it is therefore irrelevant if (as is frequently the case) the party providing initial information to the Commission which leads to an investigation may be interested in its outcome. The decision to launch an inquiry, even in such a circumstance, is fully authorized by the Act and in fact required when a sufficient showing has been made." Tidewater Radio Show, Inc., 75 FCC 2d at 678. Sections 215, 218, 220 and 403 of the Communications Act, 47 U.S.C. §§ 215, 218, 220 and 403, grant broad authority to the Commission to require the production of any and all relevant information. Reporting Lobbying Expenses By Regulated Carriers; Revisions To The Uniform System Of Accounts, 92 FCC 2d 153 (1982); Policy to be Followed in the Allowance of Litigation Expenses of Common Carriers in Rate-making Proceedings Revisions to the Uniform System of Accounts, 92 FCC 2d 140 (1982); NLT CORP., (Transferor) and American General Corp., (Transferee), For the Transfer of Control of WSM, Incorporated, Licensee of Stations WSM and WSM-FM, Nashville, Tennessee, 52 RR 2d HI 7 (1982); Petition for Issuance of a Cease and Desist Order and an Order to Show Cause Filed by ATS Mobile Telephone, Inc., Against General Communications Company, Inc., a Licensee in

Moreover, if the Commission is to adopt new policies or rules to combat dangerous corporate misbehavior, it is very clear that it must be prepared to explain and justify them should they be challenged. The Commission cannot “escape its responsibility to present evidence and reasoning supporting its substantive rules by announcing binding precedent in the form of a general statement of policy.”¹⁰⁷ The Commission must be prepared with evidence and reasoning to support its imposition of a new rule or policy.

VI. THE COMMISSION SHOULD ADOPT RULES THAT ESTABLISH NEW GUIDELINES FOR TELECOMMUNICATIONS CORPORATE BEHAVIOR

The Commission is under a “duty to evaluate its policies [and rules] over time to ascertain whether they work”¹⁰⁸ and “should stand ready to alter its rule[s] if necessary to serve

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the Business Radio Service, 49 RR 2d 947 (1981) (inquiry commenced under Section 403 specifically “to determine the full facts and circumstances concerning the operation and use of the radio paging facility owned by GCC . . . and to determine whether a sufficiently substantial basis exists warranting the institution of the revocation and cease and desist proceedings ATS has requested”).

Moreover, a finding that a company or companies violated the **law** is not a condition precedent to the convening of a Section 403 investigation. **The** Commission has often used Section 403 when misconduct or endemic public interest issues infect several firms in an industry, and even when no disqualifying misconduct is involved. See, e.g., Payola Inquiry, 42 RR2d 847 (1978) (systemic use of off the books payments to radio station officials and announcers in exchange for airplay); Domestic Telegraph Service, 25 RR 919 (1963) (telegraph service quality); Chicago Local Television Programming Inquiry, 22 RR 1021 (1962) (program service by local broadcasters); Network Investigation, 21 RR 83 (1961) (networks’ influence over program acquisition, production and distribution); Orders No. 79 and 79-A, 8 FCC 589 (1941) (newspaper/radio crossownership).

¹⁰⁷ *Rechtel v. FCC*, 957 F.2d 873 (D.C. Cir. 1992).

¹⁰⁸ *FCC v. Nat’l Citizens Comm. for Broad.*, 436 U.S. 775, 814 (1978).

the public interest more fully.”¹⁰⁹ WorldCom merely serves as a primary focal point for the need for Commission action in this arena.

The Communications Act itself provides for regular Commission review (and the potential modification) of all regulations issued under the Act applicable to the operations or activities of any telecommunications Carrier.¹¹⁰ “[I]t is clear that Congress intended that the Commission regularly evaluate its rules to determine whether they could be modified or eliminated in light of the rapidly changing, and increasingly competitive, market conditions that the 1996 Act sought to produce.”¹¹¹ This petition demonstrates, by way of WorldCom, the increased need for Commission oversight of business practices in this post-1996 “rapidly changing, and increasingly competitive” marketplace.¹¹²

A. WorldCom’s Actions Require a Stricter Application of Character Qualification Standards

In light of WorldCom’s extreme violation of public trust and flagrant misrepresentations to the Commission, the Commission should take the opportunity to review and strengthen the character qualification requirements it applies to all FCC licensees.¹¹³

¹⁰⁹ FCC v. WNCN Listener’s Guild, 450 U.S. 582, 603 (1981).

¹¹⁰ 47 U.S.C. § 161.

¹¹¹ Section 257 Report to Congress (Identifying and Eliminating Market Entry Barriers For Entrepreneurs and Other Small Businesses), 15 FCC Rcd 15376, 15440 (2000).

¹¹² Id. See also, Implementation of the Subscriber Carrier Selection Changes Provisions of the Telecommunications Act of 1996 Policies and Rules Concerning Unauthorized Changes of Consumers Long Distance Carriers, 15 FCC Rcd 15996, 16003 (2000) (*reserving the right to re-evaluate its rules on slamming “if we detect an inordinate increase in slamming after [the E-Sign Act and Letter of Agency rules] take effect”*).

¹¹³ See MCI Telecommunications Corp., 3 FCC Rcd 509 (1998) (*concluding that the Character Policy qualifications, while adopted for the broadcast licenses, provide guidance for common carrier considerations*); See also MCI Telecommunications Corporation; For Authority to

Traditionally, the Commission evaluates the character qualifications of applicants for FCC licenses by considering the three classes of non-FCC misconduct discussed above: (1) adjudicated fraudulent statements to another governmental unit; (2) criminal convictions involving false statements or dishonesty; or (3) adjudicated violations of anticompetitive or antitrust laws in connection with station-related misconduct.¹¹⁴ However, these classes of misconduct will not always provide the Commission with an adequate opportunity to target those individuals or companies that display a pattern of disregard not only for the **rules** and regulations, but basic business ethics. Rather, these classes of misconduct require an applicant or licensee be caught, tried and convicted before the FCC can protect the public interest. By the time a court adjudicates the matter, the harm to the public is done. The Commission should seize this opportunity to provide a more useful and complete guide as to what it expects in ethical behavior.

The Commission has expanded its consideration of character qualifications when circumstances merit. In the *Character Qualifications Modification* proceeding, the Commission found the three classes of non-FCC misconduct “overly narrow”¹¹⁵ and stated that “upon further reflection, we believe a propensity to comply with the law generally is relevant to the Commission's public interest analysis, and that an applicant's or licensee's willingness to violate

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Construct, Launch and Operate a Direct Broadcasting Satellite System at 110 [degrees] W.L., 14 FCC Rcd 11077, 11086 (1999) (“prior misconduct can have a material bearing on qualifications for non-broadcast as well as broadcast licensees”).

¹¹⁴ Character Policy Qualifications, 102 FCC 2d at 1209-10.

¹¹⁵ Further Character Policy Statement. 5 FCC Rcd at 3252.

other laws, and in particular to commit felonies, also bears on our confidence that an applicant or licensee will conform to FCC rules and policies.”¹¹⁶ Even so, the Commission has never promulgated ethical behavior guidelines specially tailored to the telecommunications industry and its public trust.

Although some of the details and the entire scope of the fraud committed by WorldCom remain to be fully adjudicated, the flood of information now deluging the public and investigative government entities demonstrates that WorldCom is not “possessed of the requisite propensity to obey the law.”” The Commission must have a clear mechanism in place that will allow it to ferret out such propensities at the fore as well as the aft

B. The Commission Should Adopt a Code Establishing Benchmarks for Behavior in the Marketplace

While deregulation has for the most part been good for the provision of telecommunications services, it cannot be allowed to erode the Commission’s regulation of unethical business activities while increasing corporate power and influence. Without such oversight, the business activities of those who operate with the privilege of its authorization can lead to irreversible impact on the nation’s social fabric and the global economy. A properly implemented code or guidelines of practice can affirmatively establish benchmarks for behavior in the marketplace. Applied consistently, such a code will not only encourage, but require Commission licensees and permittees to conduct themselves in ways that benefit not just themselves, but consumers and the national and global economy as well

¹¹⁶ Id.

¹¹⁷ Id.

To be effective, the code must be written in plain precise, unambiguous language so that it delivers the guidance required at the operational level. A code written in this fashion will instill notions of fairness, and enhance its credibility. Failure to write the standards in such a fashion will allow for varied interpretations and frustration of intent.

The code must contain provisions creating penalties for non-compliance. Only through the ability to impose penalties will the Commission possess the ability to cause compliance.

The code must also provide for periodic review and amendment. Periodic reviews provide the opportunity to revise and strengthen the code as necessary.

OC-UCC believes the proposed §403 investigation will demonstrate the need for several such rules and provide direction as to what specific measures would be right for the needs identified. Nevertheless, to start discussion and perhaps suggest a direction based on revelations respecting some abuses already admitted, OC-UCC proposes the following principles as suggestions of where the investigation might lead:

- Funds and/or assets will be utilized solely for a lawful and proper purpose in furtherance of its telecommunications charter, and no transfer *or* expenditure of such funds or assets shall be undertaken unless the stated purpose is, in fact, the actual purpose, the transfer or expenditure is authorized in writing and is for the purpose of advancing the telecommunications services authorized by the Commission. No undisclosed or unrecorded fund or asset shall be established for any purpose.
- No false or artificial entries shall be made in the books and records of an entity authorized or any of its subsidiaries or companies for any reason, and no employee shall engage in any arrangement that results in such a prohibited act.
- No document shall be destroyed in anticipation of a request for those documents from any government agency or court. Documents include, but are not limited to, physical records and electronic media such as disks, computer stored information and e-mail transmissions.

- No historical document or record shall ever be altered
- No employee, consultant, or agent shall ever make any untrue or misleading statement to any government investigator.
- No employee, consultant or agent shall ever seek to influence any employee or any other person to provide untruthful information to any company or government investigator, or to provide any incomplete, false or misleading information
- **All** Commission regulatees must adopt Corporate Governance Principles subject to Commission review and approval.
- Failure to adhere to the Corporate Governance Principles shall subject the regulatee to enforcement action including, but not limited to liability for forfeiture.

Finally, in conjunction with the Securities and Exchange Commission (“SEC”), the Commission should adopt rules governing auditor independence and the issuance of stock options to officers and directors. At a minimum those rules should require that:

- The external auditors of its regulatees be independent of the regulatee in accordance with SEC Regulation S-X, Rule 201 and the provisions of the Sarbanes-Oxley Act. The Commission’s rules should be based on the principle that the auditor must be independent both in fact and appearance
- External auditors should be permitted to only provide audit and audit related services and may be retained for a period of no more than five (5) consecutive years and may not succeed themselves for a minimum period of five (5) intervening years. The external auditor should be prohibited from providing the following categories of services:
 - Tax compliance
 - Tax consulting services (including tax planning)
 - Treasury advisory services
 - E-commerce advisory
 - Corporate finance advisory

- Risk management and internal control projects
 - Consultancy (all other non-audit services)
 - Appraisal or valuation services, fairness opinions or contribution in kind reports
 - Internal audit outsourcing services
 - Financial information systems design and implementation
 - Bookkeeping or other services related to the accounting records or financial statements
 - Management functions
 - Executive recruiting and human resource services
 - Broker or dealer, investment adviser or investment banking services
 - Legal services and expert services unrelated to audit
 - Any other service that the Commission determines is not permissible.
- The Commission might also require that telecommunications carriers rotate the lead partner or its auditing firm every two years. Other key partners signing off on audit opinions might be required to rotate as well.
 - The Commission's regulatees should be prohibited from hiring partners of the external auditor involved in the audit for a period of two years following termination of employment with the external auditor. Likewise, external auditors should be prohibited from hiring senior management of a regulatee for involvement in that entity's audit within a similar two-year period.
 - The regulatee's audit committee should be required to annually conduct a review of the external auditor's independence and to certify the satisfactory completion of that review to the Commission. Any independence or conflicts of interests must be reported to the Commission within thirty days of discovery.
 - Members of the regulatee's audit committee should be required to rotate off of the committee on a regular basis and the committee must be made up of independent directors.

The Commission, again in conjunction with the SEC, should enact new requirements for publicly traded companies, including:

- Shareholder approval of stock option compensation plans
- Telecommunications companies might only be permitted to use stock option incentive compensation when they are indexed to improvements in general industry performance, rather than company share value or seeming improvements in individual company performance
- A vesting period of not less than five years for any grant of stock options to officers and directors
- Holding periods for stock acquired by an officer or director (for example, 25% of acquired stock shares may not be sold during the six month period following acquisition and 50% may not be sold during the three year period following acquisition).

Adoption of rules in this arena could serve to eliminate manipulation of stock prices for short-term gain and key their value to long-term advancement of the telecommunications industry

The fact that one agency has regulated an area (or may do so in the near future) does not bar another from doing likewise. The Commission and the Equal Employment Opportunity Commission ("EEOC") have long regulated the area of equal employment opportunity. Recognizing that the two agencies had rules "directed toward a common goal and covering much the same area." in 1978 they entered into a Memorandum of Understanding so as to foster "cooperation and coordination [and] to increase the effectiveness of each agency's equal employment responsibilities and reduce possible duplication of effort..""* In connection with the

¹¹⁸ See Memorandum of Understanding between the Federal Communications Commission and the Equal Employment Opportunity Commission *Report and Order*, 70 F.C.C. 2d 2320 (1978).

adoption of OC-UCC's proposed rules, the Commission should explore entering into a similar agreement with the SEC pursuant to which the two agencies could coordinate action on charges falling within their jurisdiction.

OC-UCC. wishes to emphasize that it claims no special expertise in developing principles of corporate governance and financial dealing that will serve the goals of the Communications Act or the needs of the Commission. It offers the foregoing suggestions merely as that – suggestions that might serve as a starting point for Commission consideration based upon the facts and revelations discovered in the process of conducting its Section **403** investigation. OC-UCC. believes that **if** the Commission will undertake this **task**, it **will** find the proper model for correcting and preventing abuse destructive to a thriving telecommunications industry capable of providing for all the people of the United States a rapid, efficient, nationwide and world-wide communication service with adequate facilities at reasonable charge.

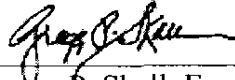
VII. CONCLUSION

Wherefore, the premises considered, Office of Communication: Inc. respectfully requests that the Commission adopt and release a Notice of Proposed Rulemaking seeking comment on the establishment of new standards of conduct applicable to all telecommunications providers receiving authorizations from the Commission and that it initiate a Section 403 investigation to enable it to develop a more complete record

Respectfully submitted,

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